STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

DRAFT

Date Introduced:	**02/18/11**	Bill No:	**Assembly Bill 1044**
Program:	**Registered Warrants**	Author:	**Butler**
Sponsor:	**Board of Equalization**	Code Sections:	**GC 17280.1 & 17280.2**
Related Bills:	**SB 120 (Anderson)**	Effective Date:	**01/01/12**

BILL SUMMARY

This bill provides that the Board of Equalization (BOE) shall accept registered warrants as payment for any tax, surcharge, or fee liability to the BOE if the registered warrant is issued specifically to that tax, fee, or surcharge payer.

ANALYSIS

CURRENT LAW

Existing Chapter 2 (commencing with Section 17200) of Part 4 of Division 4 of Title 2 of the Government Code provides that the Controller is responsible for issuing warrants drawn from the General Fund for payment of obligations of the state. In instances where the amount payable out of the General Fund is in excess of the balance remaining in the General Fund after deducting amounts earmarked or reserved for payment by law, the Controller can issue a "registered warrant."

A registered warrant carries a promise to pay the bearer the amount shown on the warrant plus interest, by a date prescribed on the warrant, usually within one year of the date of issuance. Registered warrants bear interest at a rate fixed by current state law from the date of registration to the date of maturity, or the date upon which the State Treasurer advertises that they are payable upon presentation if they bear no date of maturity.

Under existing law, there is no statute that requires the BOE to accept registered warrants. Government Code Section 17280.1 does require the Franchise Tax Board (FTB) to accept registered warrants as payment for personal income or bank and corporation taxes.

The BOE does, however, have the authority to accept registered warrants as payment of liabilities at its own discretion. Statutes in the Government Code (GC) provide that registered warrants issued by the State *may be* used as security for public or private debts (GC Section 17203), and are considered to be "negotiable instruments" (GC Section 17205). Section 17203 states: "Such registered warrants are acceptable and may be used as security for the faithful performance of any public or private trust or obligation or for the performance of any act, including the use of such registered warrants by banks and savings and loan associations as security for deposits of funds of any county, municipal or public corporation, district, political subdivision, or state agency." Section 17205 provides, "Notwithstanding any provision of the Uniform Commercial Code, all registered warrants are negotiable instruments." Under this body of law, a "negotiable instrument" is a form of payment that *may* be accepted by the payee in a particular transaction. A negotiable instrument however, is not the same as

"legal tender," which *must* be accepted as a form of payment. Based on these statutes and the lack of any legal authority that clearly prohibits it, State-issued registered warrants *could be* accepted by the BOE as valid remittances for purposes of crediting payment of a tax, surcharge, or fee liability for the "payee."

The BOE has no legal obligation or authorization to accept a registered warrant from a third party; that is, a taxpayer or entity other than the payee named on the warrant. Existing BOE practice and procedures do not allow a taxpayer to make a payment using a third party check, due to the increased possibility of fraud inherent in such a transaction. The same concerns would apply to third party registered warrants.

PROPOSED LAW

This bill would amend GC Sections 17280.1 and 17280.2 to require the BOE to accept registered warrants from a taxpayer with any tax, surcharge, or fee obligation owed when the registered warrant has been paid directly to that tax, surcharge, or fee payer.

This change would eliminate any future ambiguity on the issue and allow BOE staff to immediately implement plans to accept and process any registered warrants and thereby avoid any future uncertainty on whether or not an outstanding liability may be satisfied in that manner.

This bill would also delete confusing language in subdivision (c) of Section 17280 related to a taxpayer receiving interest on a registered warrant. Currently, if a taxpayer submits the warrant before it matures (redeemable), the taxpayer does not receive any interest. The current language can be misleading since taxpayers may incorrectly read it to mean they are entitled to interest from the issue date of the warrant to the taxpayer to the date the taxpayer submits the warrant as payment of tax. The proposed changes to Section 17280.1 protect a taxpayer's right to receive interest on a mature warrant.

Background

On June 24, 2009, the State Controller announced a plan to begin issuing registered warrants in order to manage the State's cash crisis. The last time the State of California was forced to issue registered warrants was in 1992 and the BOE Members voted at its August 27, 1992 meeting to accept state-issued registered warrants for payment of taxes.

To respond to the Controller's 2009 announcement, the BOE Members asked the BOE's Legal Department whether the BOE would be allowed to accept registered warrants issued by the state in payment of tax liabilities from taxpayers who are payees on registered warrants. The following explains the Legal Department's opinion on this issue:

The BOE is not required to accept registered warrants. There is no law requiring the BOE to accept registered warrants. There is, however, a statute (GC section 17280.1, added by Chapter 1211, Statutes of 1983) that requires the State to accept registered warrants as security for payment of personal income taxes or bank and corporation taxes, meaning that it applies only to the Franchise Tax Board.

While the BOE is not obligated to accept registered warrants, it is not prohibited from doing so.

The BOE has discretion to accept registered warrants. There is no specific statutory or constitutional provision authorizing a State agency or the BOE to accept a registered warrant as payment. The statute applicable to payments to the BOE, Revenue and Taxation Code (RTC) Section 7101, provides that all fees, taxes, interest, and penalties imposed and all amounts of tax required to be paid to the state under Part 1 of the Sales and Use Tax Law shall be paid to the BOE in the form of *remittances* payable to the BOE of the State of California. The term "remittances" is not defined by statute. Based on the foregoing, there is nothing requiring the BOE to accept registered warrants issued by the State as a "remittance."

Nevertheless, statutes in the Government Code provide that registered warrants issued by the State may be used as security for public or private debts (GC section 17203) and are considered to be "negotiable instruments" (GC section 17205).

Section 17203 states: "Such registered warrants are acceptable and may be used as security for the faithful performance of any public or private trust or obligation or for the performance of any act, including the use of such registered warrants by banks and savings and loan associations as security for deposits of funds of any county, municipal or public corporation, district, political subdivision, or state agency." Section 17205 provides, "Notwithstanding any provision of the Uniform Commercial Code, all registered warrants are negotiable instruments." Under this body of law, a "negotiable instrument" is a form of payment that *may* be accepted by the payee in a particular transaction. A negotiable instrument however, is not the same as "legal tender," which *must* be accepted as a form of payment.

Based on these statutes and the lack of any legal authority that clearly prohibits it, the State-issued registered warrants *could be* accepted by the BOE as valid remittances for purposes of crediting payment of a tax, surcharge, or fee liability for the "payee."

Legislative Proposal. In response to the analysis provided by the BOE's Legal Department, the BOE Members directed staff at the July 21, 2009 BOE hearing to accept the state-issued registered warrants as payment of sales and use taxes and other taxes, surcharges, or fees owed to the BOE. The BOE Members also directed staff to draft a legislative proposal that would clarify in law the BOE's current practice to accept registered warrants.

At the August 31, 2009 BOE Legislative Committee meeting, the Members voted unanimously to support a proposal that would give the BOE the same exact authority as the FTB. The proposal would require the BOE to accept registered warrants as payment for any tax, surcharge, or fee liability to the BOE if the registered warrant is issued specifically to that tax, fee, or surcharge payer.

The legislative proposal was incorporated into the BOE-sponsored omnibus bill, SB 1494, during the 2010 Legislative Session. However, in the Assembly Appropriations Committee the bill was recommended for the suspense file because of the registered warrant provisions. In order to move the BOE-sponsored bill off suspense, the BOE staff accepted the Committee recommendations to eliminate the registered warrant provisions from the bill.

COMMENTS

1. **Sponsor and Purpose.** This bill is sponsored by the BOE in order to codify the BOE's current administrative practice to accept registered warrants as payment for tax liabilities. Current law requires the FTB to accept payment by registered warrants from a taxpayer. However, BOE is not required to accept registered warrants, but is not prohibited from doing so. Having clear statutory authorization to accept registered warrants would eliminate any future ambiguity. And, given that the fiscal situation of the State may necessitate further use of registered warrants, it will be clear that the BOE is required to accept them as payment.

2. **BOE already has procedures in place for taxpayers to pay with registered warrants.** During 2009, the BOE accepted State-issued registered warrants as payment of sales and use taxes and other taxes and fees owed to the BOE. Because procedures already exist to allow taxpayers to pay with a registered warrant, implementing the bill's provisions do not pose any problem for the BOE.

3. **Related legislation.** SB 120 (Anderson) would require a state agency, upon the Controller making a specified determination, to accept a registered warrant issued by the Controller for payment of any state obligation.

   AB 1506 (Anderson) of the 2009-10 Legislative Session contained the same provisions as SB 120. The BOE Members, at the August 31, 2009 BOE Legislative Committee meeting, unanimously voted to support July 1, 2009 version of AB 1506 which would have required a state agency to accept registered warrants for payment of state obligations. AB 1506 was vetoed by Governor Schwarzenegger on September 30, 2010, with the following veto message:

   > "This measure would require all state departments, upon a specified determination made by the State Controller's Office, to accept registered warrants, also known as IOUs, in lieu of cash payments. The issuance of IOUs represents an embarrassing failure on the part of the state to manage its finances. Unfortunately, if the Legislature does not pass a balanced budget soon, the possibility that the Controller will be forced to issue IOUs this year becomes all too real. I sympathize with businesses that were issued IOUs last year and those businesses that may receive them this year. IOUs place enormous financial strains on recipients who are unable to use them to pay their own obligations, including debts owed to the state. However, requiring state departments to accept IOUs in lieu of cash payments defeats the purpose of issuing IOUs in the first place. It would exacerbate the state's cash crisis and would accelerate the possibility of the state defaulting on its debt service and payroll obligations.
   >
   > Since IOUs could be avoided if the Legislature passed a balanced budget, I am unable to sign this bill."

COST ESTIMATE

Because the BOE is already accepting registered warrants as payment for outstanding liabilities, this measure would have no administrative cost impact.

REVENUE ESTIMATE

This bill would have no impact on state and local revenues, as well as any special fund revenues. However, because payment of taxes, fees, and surcharges using a registered warrant would require the warrant to be held until the warrant redemption date, there could be a deceleration of cash receipts.

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This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the BOE's formal position.